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Aswath Damodaran, Kose John, Crocker H Liu

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Aswath Damodaran, Kose John, and Crocker H. Liu*

Leonard N. Stern School of Business, New York University, NY, NY 10012-1126

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1. Introduction

One of the central concerns of corporate governance is the degree of alignment of managerial incentives with that of shareholder interest (see Schleifer and Vishny (1997)). Although this issue has been extensively studied in the literature on agency theory and corporate governance¹, direct empirical testing of the degree to which managerial incentives are aligned with the shareholder interest has been difficult. We focus on different organizational forms where the associated structure of contracts differ greatly in the managerial discretion and the amount of free cash flow available to management. Changes among these organizational forms can potentially cause a conflict of interest between managerial incentives and shareholder wealth maximization. In this paper, we examine whether managerial incentives or shareholder wealth maximization drive the choice among organizational forms.

Although there has been some theoretical analysis of agency considerations in organizational choice, little empirical work on the topic exists.² One of the obstacles in doing empirical work on the choice of organizational forms is the difficulty of controlling for the varied factors that might influence organizational choice (e.g., different regulation,

¹The structure of contracts and the associated agency problems influence the choice of organizational forms. [see Alchian (1950), Fama and Jensen (1983a,b)]. More specifically, Fama and Jensen (1983b) emphasize the role of the control of agency problems as a major determinant of the structure of organizations. Agency problems arise because of costly contracting. Associated costs include the costs of structuring, monitoring and bonding a set of contracts among agents with conflicting interests, plus the residual loss incurred because the cost of enforcing contracts exceeds the benefits. See Jensen and Meckling (1976). For a survey of the literature in this area, see Jensen and Smith (1985) and Barnea, Haugen and Senbet (1985). Allen and Winton (1994) survey the design of optimal financial contracts.

² Brickley and Dark (1987) provide the notable exception. They present evidence that agency-related problems determine the trade-off between owning (operating centrally) and franchising. The cost of monitoring store managers appears to be especially important. Three other papers that examine related issues are Mayers and Smith (1981), Masulis (1987), and Karpoff and Rice (1989). Thirty firms in the life insurance industry that switched from a common stock to a mutual ownership structure are examined in Mayers and Smith. The authors conclude that the change is efficiency-enhancing on average and no group of claimholders systematically loses. Masulis examines mutual savings and loans that switch to a stock charter. Karpoff and Rice study 13 corporations established under the Alaska Native Claims Settlement Act of 1971 (ANCSA). These corporations have many organizational restrictions, the most important of which is that stock cannot be traded. The authors document poor financial performance, a high incidence of

products and technology). However, in the real estate industry, we are able to find that different organizational forms exist side by side to undertake basically the same activity. These organizational forms have contract structures which seem to allow for widely ranging degrees of managerial discretion. Moreover, in our study, we examine firms making changes in their organizational forms. By confining ourselves to a given industry and focusing on changes in organizational form made by existing firms, we are able to hold constant many factors which might have a bearing on organizational choice.

Real estate firms can take on a number of different organizational forms. At one extreme, they can be real estate investment trusts (REITs), paying no taxes but accepting in return significant restrictions on investment policy. In addition, the legally mandated requirement that the firm pay out 95% of its taxable earnings to shareholders significantly limits the free cash flow under managerial control. At the other end of the spectrum, the traditional corporate form allows much greater freedom to make investment and dividend decisions, but at the significant cost of double taxation. In between, there are organizational forms such as master limited partnerships (MLPs) and business trusts, which share some characteristics with both REITs and corporations.³ The wide range of managerial discretion allowed by these organizational forms correspondingly allow for a wide range of agency costs. Since these organizational forms coexist in the real estate industry, a natural question which arises is what managerial objectives drive changes among these organizational forms. Does managerial self-interest determine the changes among these organizational forms or management's concerns for maximization of shareholder wealth? What bearing does the degree of alignment of manager wealth and

control contests, and high turnover among directors and managers in these ANCSA firms.

³ Moore, Christensen, and Roenfeldt [1989] investigate MLPs formed from total conversion of corporate assets and rolling out subsets of those assets, and document a significant positive announcement effect.

shareholder wealth (represented by the fraction of stock ownership by insiders) have on these choices? Alternatively, is the degree of alignment of managerial incentives and shareholder interest weak or strong? If they are weak, managerial objectives would drive changes among organizational forms. If they are strong, shareholder wealth maximization would drive changes in organizational forms. Whether the degree of alignment is strong or weak is an empirical question.

We examine changes among four different types of organizational forms, namely REITs, MLPs, business trusts and corporations. To address whether managerial incentives or shareholder value is the major motivation for these organizational form changes, we classify these changes in two categories. In the first category, we have changes in organizational form which move the firm from a tighter structure, say REITs, to a looser structure, say corporations. In these changes, the managerial discretion increases. In the second category, we include organizational form changes from a looser structure to a tighter structure. In these changes, managerial discretion decreases. The presence of changes in the second category makes it plausible that managerial incentives are not the only motivating factor behind these organizational changes. However, since these changes are initiated and carried out by managers with only routine approval by the shareholders, we believe that it is important to examine the wealth effects of different types of organizational form changes.

To examine which of these hypotheses holds, we examine the stock price reactions to all organizational form changes. We find that, on average, announcements of organizational changes, whether from a looser to a tighter structure, or vice versa, are accompanied by higher stock prices. This would suggest that stockholders perceive themselves to be better off after these changes. We also classify firms, based upon

whether total management compensation increased or decreased after the organizational change, and find that stockholder wealth increases in both groups. We then track the stock price and profitability measures for the firms that change organizational form for two years before and after the changes, and document that firms become more profitable and valuable after organizational changes. This would suggest that the initial perception of stockholders is borne out by the subsequent facts. Finally, we provide evidence that the firms that changed their organizational form were, on average, different than the real estate firms that did not change their organizational form in terms of profitability, cash flow generating capacity, and overall financial health.

This paper is organized as follows. In section 2, we present the institutional description of the different organizational forms and the restrictions on each and present the hypotheses and testable implications for both the stockholder wealth maximization and managerial interests hypotheses. In section 3, we describe the sample and illustrate the impact that organizational form changes have on stock price. We also follow up and examine the profitability and stock price performance of real estate firms around organizational changes. Section 4 discusses our results, and section 5 concludes.

2. Institutional background

In this section, we describe the characteristics of the various organizational forms that are the subject of this study - real estate investment trusts, master limited partnerships, business trusts, and real estate corporations.

2.1. Salient differences between organizational forms

There are three major areas in which the real estate organizational forms examined in this study differ.

- *Structure of Taxation - Single vs. Double Taxation:* Single taxation is a characteristic of REITs and MLPs since both are taxed only at the investor level but not at the firm level. This tax benefit is given to REITs to compensate for certain investment and dividend policy restrictions that REITs have to adhere to. MLPs, in contrast, receive single taxation status only if they invest in certain activities such as real estate or oil and gas, otherwise MLPs are treated as a corporation for tax purposes. This tax advantage does not exist for business trusts and corporations which are taxed at the entity level on income and also at the investor level on dividends.
- *Restrictions on Investment and Dividend Policy - More Restrictive to Less Restrictive:* The tax code requires REITs to distribute 95% of their taxable income to shareholders. The code further requires that a minimum of 75% of a REIT's gross income must come from real estate. A REIT is further restricted to be a passive investment conduit; as such less than 30% of a REIT's income must come from the operation of real estate held less than 4 years and income from the sale of securities held less than 1 year. REITs also cannot engage in active real estate operations including operating a business, developing or trading properties for sale, and selling more than 5 properties per year. A REIT is further prohibited from entering into tax-free exchanges to acquire properties. To ensure the passive nature of REITs, the tax code had required REITs to use independent contractors to manage properties. This direct management restriction was removed in the 1986 tax reform act.

Although no dividend payout restrictions exist for MLPs in contrast to REITs, a high payout ratio is likely, given that partners are taxed regardless of whether they actually receive the income or the MLP retains it. This has to be weighed off against the investment opportunities that the MLP has. The empirical evidence suggests that

MLPs do pay out a high proportion of their earnings as dividends. While MLPs are restricted to engage in real estate activities (or oil and gas), there are no restrictions as to the nature or management of these activities. Consequently, MLPs can actively and directly engage in the real estate trade or business. No MLP restrictions also exist on the number of properties that can be sold in any given year.

Business trusts and corporations have no restrictions on dividend payout and can engage in any real estate or non-real estate activity except those prohibited in the declaration of trust or corporate charter respectively.

- *Managerial Discretion over Cash Flows-Less to More Managerial Discretion:* Managers of REITs have less discretion over what to do with their cash flows relative to other real estate organizational forms given the dividend payout requirements and investment policy restrictions associated with REITs (See Jensen (1986)). The flexibility afforded MLP managers are greater than that of REITs since the partnership agreement of most MLPs specify only minimum cash payouts and do not mandate specific payout ratios (see Moore et al., (1989)). Business trusts offer even more managerial flexibility than either of the previous two organizational forms with respect to the disposition of cash flows. This flexibility arises as the result of no payout restrictions although the managers of business trusts have unlimited liability for all debts of the trust. At the opposite end of the spectrum, managers of corporations have the most control over their cash flow options since there are no payout or investment restrictions.

Based on these preceding dimensions, changes in organizational form are classified as (a) moves to a looser structure, or (b) moves to a tighter structure. More specifically,

the movement of a REIT to a business trust, a business trust to a corporation, REIT to a corporation, REIT to a MLP, and a finite REIT⁴ to MLP are classified as shifts to a looser structure. A shift from a corporation to either a REIT or MLP and a change from an MLP to a REIT in contrast, are classified as moves to a tighter structure.

From the description of organizational changes provided in this section, changes in organizational form change the entity-level tax status, the level of managerial discretion and restrictions on investment and dividend policy. These changes can be motivated by the desire to increase stockholder wealth or may be initiated by management to serve their own interests. In the following sub-sections, we will examine these hypotheses and the predictions that would emerge from each of them.

2.2. A Shareholder Wealth Maximizing Rationale for Organizational Changes

Given the description of organizational forms provided in this section, the trade-off is between the greater tax benefits and reduced agency problems associated with organizational forms such as REITs, and the restrictions on investment and dividend policy that come with these benefits. In general, we would expect firms that are losing money and have negative cash flows to value flexibility more than any loss of tax benefits and increased agency problems. These firms are more likely to shift from a tighter organizational form to a looser one in order to maximize shareholder wealth. In contrast, we would also expect firms with large earnings and positive cash flows to give much more weight to single taxation benefits and agency problems than to the value of flexibility, thus making it more likely that they will shift to a tighter structure.

⁴ A finite REIT is created with a finite lifetime in mind, at the end of which the assets it owns are liquidated and the cash is returned to the stockholders.

2.3. A Managerial Rationale for Organizational Form Changes

While wealth maximization may be the rationale for the observed organizational changes, a case can be made for the hypothesis that these changes are motivated by side benefits to the insiders who run the firm rather than by the objective of maximizing stockholder wealth.

Consider, for instance, the firms that switch from a tighter to a looser organizational structure. Real estate investment trusts restrict managerial discretion at two levels. First, the requirement that 95% of the earnings be paid out as dividends reduces the free cash flow available for managers to reinvest. Second, the restrictions on investment policy constrain them even on the limited funds that they have available after dividends. An argument can be made that the managers of a real estate investment trust may push for a change to the corporate form, the tax disadvantage notwithstanding, in order to have access to more of the cash flow and to invest in a wider array of projects.

For firms that switch from a looser to a tighter structure, the incentives from a managerial standpoint are different. Here, managers and insiders may be willing to accept the restrictions on dividend and investment policy, if the organizational change allows them to increase their overall compensation. REITs often have arrangements where insiders receive additional benefits as property managers or advisers; these arrangements may be more difficult to hide in the corporate form.

An alternative way of characterizing the managerial interest hypothesis is that the mechanisms to align the managerial interest with that of the shareholders is not sufficiently effective such that managerial preferences for discretion outweigh the impact on their wealth through the compensation structure. In this case, rational managers given the compensation structures in place would implement organizational form changes

which are consistent with their preferences even when it is not in the shareholder interest. In the cases where the compensation structures are able to align managerial interests with that of the shareholders, the impact of the organizational change on the manager's wealth dominates his preference for discretion. As an example, when the fractional ownership of equity of the manager is high, it is possible that the impact of an equity-value-increasing organizational change on the manager's wealth aligns him sufficiently with the interest of the shareholders.

2.4. Testable Implications

Are organizational changes motivated primarily by managerial incentives or stockholder wealth maximization? While a case can be made for each, there are several implications that emerge from each of these hypotheses that are testable.

1. Type of Firms making Organizational Changes: If stockholder wealth maximization is the reason for organizational changes, we would expect to see firms in financial distress, with low cash flows and earnings, switching from tighter to looser structures to take advantage of the flexibility. If managerial interests are motivating the organizational changes, we would expect to see firms with significant earnings and cash flows changing from tighter to looser structures, since the benefits of controlling the free cash flow is greatest in these firms.

Looking at firms which switch from a looser to a tighter structure, we would expect firms with high earnings and poor investment opportunities to do so, if the motivation is stockholder wealth maximization. The tax benefits overwhelm the lost flexibility in these cases. Conversely, if managerial interests motivate the changes, we would expect these changes to occur in firms where the potential for side-benefits from managerial or advisory interests is greatest.

2. Stock Price Reaction to Organizational Changes: This is clearly the strongest test of the two hypotheses. If stockholder wealth maximization is the perceived reason for organizational changes, stock prices should go up on the announcement of these changes. This should be true whether the change is from a tighter to a looser structure or from a looser to a tighter structure. If, on the other hand, management interests are perceived to be served by these organizational form changes, at the expense of stockholder wealth maximization, stock prices should go down on the announcement of organizational changes. In testing these hypotheses, we should note that it is entirely possible that both managerial interests and stockholder interest are served by the organizational change. Thus, the fact that the stock price goes up on the announcement of an organizational change is consistent with the stockholder wealth maximization hypothesis, but does not, by itself, constitute proof that managerial interests are not also being served simultaneously.

3. Effects of Change on Profitability and Wealth: This is a test of whether the initial perceptions of investors (which determine the stock price reaction on the announcements) are borne out by subsequent changes in profitability and stockholder wealth. In other words, if the changes, on average, are motivated by stockholder wealth considerations, then firms should become more profitable and valuable after these changes. If, on the other hand, they are motivated by managerial interests, then firms will become less profitable and valuable after these changes.

3. Sample description, methodology and results

The sample is described in section 3.1. In section 3.2, we compare the characteristics of firms that move to a tighter structure with the characteristics of firms that move to a looser structure. The market reaction to the announcement of changes in

organizational form is presented in section 3.3. Section 3.4 evaluates changes in the performance of firms that make organizational changes, using market value and profitability measures. In section 3.5, we examine whether the firms that made organizational changes during the period of our sample differ significantly from other real estate firms during the period that chose not to make these changes.

3.1. Sample description

Our data consists of all publicly traded real estate companies that had at least one change in their organizational form during the period from January 1966 through December 1994 and also had information available on them on both the CRSP daily return and the COMPUSTAT quarterly databases for this period. A total of 128 organizational changes fulfilled this criteria with 28 firms having more than one organizational change, first moving from a REIT to a business trust and then later shifting to a corporation, over our study period. Information on organizational restructurings was obtained from various issues of *Audit Realty Stock Review*, *REIT Factbook*, and *Moody's Bank and Finance Manual, volume 2* with the *Wall Street Journal*, 10Ks, SEC proxy statements, and/or the *PR Newswire* used to get dates of board of trustees/directors approval and shareholder approval for changes in organizational form.

Several criteria were utilized to classify our sample. First, we partitioned firms into non-distressed and distressed at the time of the organizational change by examining the *Wall Street Journal Index* for the five-year period preceding a change in the firm's organizational structure. A firm was classified as distressed if the firm not only incurred a net loss for each of the three years preceding the reorganization but also reported at least one of the following adverse events during that three-year period: (a) the firm was in technical default on their debt obligations missing two or more interest payments on any

class of debt; (b) The firm was in actual default and filed for bankruptcy protection either under Chapter 10 or 11 of the Federal Bankruptcy Act; (c) the firm asked banks/public debtholders to swap properties in lieu of debt forgiveness; (d) creditors refused to renegotiate existing credit agreements that the company stated was necessary for continued solvency; (e) the firm indicated that they would omit dividends; and (f) the firm reported that its auditor had given it a qualified opinion on the firm's financial condition. Over 86% of the firms meeting this criteria for distress were in actual or technical default in bond payments and as such were suffering severe financial difficulties. We also grouped our sample into firms moving to a looser or a tighter organizational form as discussed earlier in section 2.1.

3.2. Firm Classification and Organizational Changes

The majority of firms in our sample moved from a tighter to a looser structure rather than from a looser to a tighter organizational form. More specifically, there were 54 (42.2%) non-distressed firms and 58 (45.3%) distressed firms that moved to a looser structure. In contrast, only 16 firms (12.5%) opted for a tighter organizational form. Thus, 112 of the 128 organizational changes were to a looser structure. A distinguishing characteristic of these organizational restructurings is that all firms moving to a tighter structure were non-distressed firms, whereas all of the distressed firms moved to a looser structure. This evidence is more consistent with the "stockholder wealth maximization" hypothesis than the managerial interest hypothesis.

We expanded this analysis by doing a PROBIT on firms making organizational changes and classifying them on the basis of whether the change was to a tighter or a

looser structure. We examined differences between the two groups on the following criteria:

- Profitability at the time of the change, measured using the operating income as a percentage of total assets (E/TA)
- Leverage at the time of the change, measured using the debt as a percentage of the total assets (D/TA)
- Dividend Yield at the time of the change, defined as the annual dividend divided by the market price (DY)
- Cash Flow generating capacity at the time of the change, measured using the free cash flow to the firm prior to capital expenditures, as a percentage of total assets. The free cash flow is estimated by adding the depreciation back to the earnings before interest and taxes (FCF/TA)
- Size of the firm, measured by the book value of total assets (TA)
- Insider Holdings at the time of the change, measured as the percentage of common stock held by managers, directors and those holding more than 5% of the outstanding stock in the firm. This data is obtained from the filings made by these firms with the SEC. (INS)

The results of the PROBIT were as follows:

$$\text{NTIGHT} = 1.28 + 24.03 \text{ E/TA} - 1.08 \text{ D/TA} + 8.39 \text{ DY} + 11.23 \text{ FCF/TA} + 0.09 \text{ TA} + 4.65 \text{ INS}$$

$$(5.70) \quad (7.45^*) \quad (1.24) \quad (3.65^*) \quad (4.36^*) \quad (0.81) \quad (3.55^*)$$

(T statistics are in brackets; *: Statistically significant at 95% confidence interval)

where NTIGHT is the probability that a firm will move to a tighter organizational structure. This probit suggests that firms which switch to a tighter structure tend to be more profitable, have higher cash flows, pay more in dividends and have higher insider

holdings than firms that switch to a looser structure. For firms with high profitability and large free cash flows, there should be no change to a tighter organizational form, if managerial interests alone dominated. The payments of large dividends, even prior to the organizational change, suggests that there was a significant tax liability being borne by owners prior to the shift; since these firms were almost all corporations prior to the change, these dividends were subject to double taxation. This, in conjunction, with the high insider holdings may explain why managers would choose to restrict their own flexibility. Managers are willing to trade off the higher value of their equity ownership (through lower taxes) for the lower managerial discretion in the post-change organizational form.

Since the empirical questions relate to the conflict between stockholder and managerial interests, the question of insider ownership is worth examining in more detail. In Table 1, we provide the summary statistics on insider ownership of firms that moved to a looser structure and those that moved to a tighter structure, in the year of the organizational change.

Put Table 1 here

Note that the firms that moved to a tighter structure had a median insider holding in excess of 25% of the outstanding stock in the firm. Since these insiders are also the managers and directors⁵ of these firms, the separation of management and ownership that is at the core of the agency problem is fairly limited. This, we would argue, is the reason why the managers of these firms are willing to accept the loss of discretionary power that goes with a tighter structure. In contrast, the median insider holdings at the firms that moved to a looser organizational form is only 2.55%. There is clearly the potential here that managerial interests could be the dominant motive behind these organizational

⁵ We are aware that insiders also include anyone holding more than 5% of the outstanding stock. In all of our cases, the insiders who held more than 5% also had representation on the board or in the management of the real estate concern.

changes. In the sections that follow, we will examine whether the evidence supports this notion.

In the next section, we will examine how stockholders perceive these organizational changes, when they are announced, and whether they believe that these actions are directed towards increasing stockholder wealth.

3.3. Market reaction to organizational changes

The market reaction to announcements of changes in organizational form is studied for a number of reasons. First, it provides us with a sense of whether these changes convey information to financial markets about future cash flows and growth. Second, and more important, it is a simple test of whether these decisions are made to increase shareholder value. If they are, we would expect both groups of organizational changes, on average, to elicit positive market reactions. If, on the other hand, we do find, on average, a negative stock price response, it is entirely possible that organizational changes in some categories, at least, are made to serve managerial interests rather than stockholder interests.

The sequence for an organizational change is as follows: The board approves the change in organizational form, subject to receiving the necessary approvals from the firm's creditor banks, noteholders, and shareholders. Next, the creditor banks and bondholders vote on the proposed reorganization of the firm. After approval is obtained from the bondholders, the shareholders vote on the proposed change. This is the standard process for creating a looser structure. If the change is to a tighter structure, only board approval is required. For our sample of firms, there was not a single instance where bondholders or stockholders overruled the board of directors. Consequently, information about the board's approval is the earliest announcement⁶ of the organizational change. The stockholders' consent represents the second (and later) announcement of the same

⁶ The earliest Wall Street Journal announcement dates, for firms in our sample, are all board approval dates. Thus, it can be viewed as the earliest news release relating to the organizational change.

change. To keep the analysis clean, we checked the announcements of organizational changes for other announcements which were made simultaneously. Any announcements that were contaminated by the existence of other information were eliminated from the sample.

We examine the market reaction to both events, using event-study methodology. First, the dates of the board approval and the shareholder approval of the organizational changes are obtained from the *Wall Street Journal*. (For some of the firms in the sample, the date of board approval was not available.) Second, we estimate market model parameters, using 200 trading days. We start 220 trading days before the announcement date of the organizational change and end 21 days before the date. Third, we estimate abnormal returns for each trading day starting five days before each event and ending five days after, for each change in the sample. Fourth, we estimate the cross-sectional mean and standard error across the sample for each trading day and calculate the t-statistics.

The results of the event study are summarized and reported in table 2 for the overall sample and for the subsamples described above. There is a positive and statistically significant reaction to the announcements of board approvals for organizational changes for all the groups – non-distressed firms moving to a looser structure, non-distressed firms moving to a tighter structure, and troubled firms moving to a looser structure. This result holds whether we look at the day of the announcement, the immediate announcement period (day 0 and 1), or the entire eleven day window (days -5 to +5). There is a mixed effect following the later announcement of shareholder approval. Only troubled firms report statistically significant positive returns either on the announcement day itself or over the announcement period. Thus, the initial announcements of pending organizational changes seem to generate positive reactions, whether the shift is to a tighter or to a looser structure, while the later announcements of shareholder approval generate few significant reactions.

Put Table 2 here

A potential selection bias associated with the traditional event study methodology has been explored by Malatesta and Thompson (1985), Eckbo, Maksimovic, and Williams (1990), and Acharya (1988, 1993). They point out that if there are significant differences among firms that have information events and firms that do not, a selection bias can exist in the event study. In particular, they note that prior to events, financial markets use information about firms to evaluate the likelihood of an information event, and that the reaction to an event has to be measured relative to these prior probabilities. To illustrate, let us denote as ΔS the part of the firm-value-change that will accrue to the shareholders. Let us also assume that only a fraction of the organizational changes for which ΔS is positive actually takes place. This could be because managerial incentives and private benefits play a role as initiatives for the organizational change. The investors in the market and the shareholders at large only partially understand these factors. Prior to the announcement of the organizational change, the market assesses a probability π , $\pi < 1$, of the organizational change going through. At the announcement, the stock price goes up to reflect the incremental value, $(1-\pi) \Delta S$. The average announcement effect for the different categories of organizational form changes should be positive.

We apply the two-step approach described in Acharya (1993), in which the first step is a PROBIT, that estimates the probability of an organizational change, given information on the company prior to the change. We estimate the prior probability (ϕ_j) of an organizational change for a real estate firm from a probit analysis, run on all real estate firms with data available on an annual basis from 1973 to 1989, using the following independent variables⁷ - debt as a percentage of total assets, the dividend yield, operating incomes as a percentage of total assets and the price to book value ratio. The probit was run as follows. First, a holdout sample of 125 real estate firms which had no

⁷ The choice of variables for the PROBIT was driven largely by the hypotheses discussed earlier. The financial distress of a firm is captured by both the operating earnings/total assets and the debt ratio. The agency cost aspect is measured by the operating earnings/total asset ratio and the dividend yield. Any significant undervaluation of the assets of the firm prior to the change is captured in the price/book value ratio.

organizational changes between 1973 and 1989 was collected, and data on the variables used in the probit was obtained. Second, this sample was combined with the firms which had organizational changes over the period. Third, a probit was run, to estimate the probability of an organizational change, and the results are summarized below -

$$\phi_j = 0.25 - 61.67 (\text{Operating Earnings/TA}) + 5.12 (\text{Debt/ Total Assets}) - 6.09 (\text{Dividend Yield}) + \quad - 3.00 (\text{Price/Book Value})$$

In other words, firms with low earnings relative to total assets, high debt ratios, low dividend yields and low price/book value ratios were more likely to make organizational changes than firms that do not possess these characteristics. The probabilities (ϕ_j) estimated from these probit analyses are used in conjunction with the cumulative probabilities (Φ_j), to estimate γ_j and $\hat{\gamma}_j$, where

$$\gamma_j = \phi_j / \Phi_j \quad \hat{\gamma}_j = - \phi_j / (1 - \Phi_j)$$

In the second stage, we regress excess returns estimated during the appraisal period (ε) against γ_j and $\hat{\gamma}_j$,

$$\varepsilon = \mu + \pi (\gamma_j - \hat{\gamma}_j) + \upsilon$$

The coefficient ' π ' in the regression is a measure of the market response to the announcement of an organizational change by a real estate firm, conditioned on insiders being rational in choosing to have an organizational change. A positive π implies that the reaction ($\pi \gamma_j$) is positive, and the mean of this is the cumulated abnormal return. The bias adjusted abnormal returns are reported in the last row of panel A , table 2.

While the abnormal returns are slightly lower when the bias adjustment is made, they remain statistically significant and positive when the board announces its approval of organizational changes. The abnormal returns are not significant for the whole sample or any of the groups around the shareholder approval date. This finding is consistent with the argument that organizational changes are primarily motivated by the desire to make real changes in operating policy, thus allowing the firm to maximize the net value effect of changes in the tax shields, agency costs, and distress costs.

It is possible that the 21-day window used in the event study described above is not long enough to fully measure the market reaction to these changes. Therefore, we also estimated excess returns on a monthly basis, starting 12 months before the change and continuing through to 12 months after the change. These excess returns reveal that the positive market reactions to organizational changes illustrated in table 2 continue to persist for all the categories for the 12 months after the change.

While the evidence presented in Table 2 is consistent with the hypothesis that organizational changes are motivated by stockholder wealth maximization, it is entirely possible that managers, while increasing stockholder wealth, are also serving their own interests. To test the conflict between stockholder and managerial interests more precisely, we collected information on the total compensation received by managers at these real estate firms in the year before the organizational change and the year after. We then categorized these changes into two groups; the first group includes firms where managerial compensation increased after the organizational change and the second group includes firms where managerial compensation decreased after the organizational change. If managerial interests are the dominant objective behind organizational changes, we would expect stockholder wealth to increase less in the first group and more in the second group. We would concede two weaknesses associated with this test. The first is that we are using ex-post information rather than ex-ante information; what we would really like to measure is not the actual compensation in the year after the change but the expected compensation at the time of the organizational change. While we have information on the structure of the management contracts at the time of the change, the contracts are complex and are stated as percentages of other variables (expected revenues, income etc.) and are difficult to convert into expected dollar values. The second is that compensation is only one component of managerial utility; it is entirely possible that these organizational changes yield other shifts that serve managerial interests, such as increasing discretionary power over investment and financing decisions. Table 3

summarizes the abnormal returns for the same periods that we examined in Table 2 for the two sub-groups.

Put Table 3 here

The abnormal returns are positive and statistically significant for both sub-groups. In fact, the average abnormal return during the announcement period is 3.87% for the sub-group where management compensation increased after the organizational change, compared to only 2.13% for the sub-group where management compensation decreased. There are two interesting implications. First, the fact that the first group has a higher abnormal return suggests that if managerial interests are being served, at least in terms of compensation, it is not at the expense of stockholder wealth. Second, the fact that management compensation decreases in almost half the cases, while stockholder wealth increases, is strong evidence that stockholder wealth is a major force behind organizational changes.

In addition to examining the management compensation in the years before and after the organizational change, we also checked to see if whether the management team itself changed at the time of the organizational change. We looked at whether the CEO of the real estate firm or the management advisory team used by the firm were replaced in the year of the organizational change. The CEO was replaced in 18 of the 95 firms in our sample in the year of the change; the management advisory team was replaced in 9 of the 95 firms that had advisory teams in the first place. The number of managerial changes increases even more dramatically if we expand our observation period to the three years around the organizational change.

In summary, the large number of firms where management compensation decreases after the organizational change, as well as the significant managerial turnover around the change is supportive of the hypothesis that many, if not all, of these changes are motivated by stockholder interests. The increase in the stock price around these changes is evidence that investors perceive the organizational changes as good for stockholder wealth maximization and that they do not view them, at least on average, as

being driven primarily by managerial interests. The second point we would make, however, is that there are a substantial number of cases where managerial interests are also served by the change in organizational form.

3.4. Firm performance before and after organizational change

To evaluate whether the preceding market reactions are justified, we examine three measures of firm performance: operating income (defined as net income(NI) divided by total assets(TA))⁸, return on assets (defined as EBIT divided by total assets(TA)), and cumulative abnormal returns⁹. Each of these measures is compared two years before and two years after organizational restructurings relative to two separate classifications. The first classification is based on structural change, whether the firm shifts to a looser or a tighter structure at the time of the reorganization. The other firm classification consists of financial health at the time of the change (non-distressed versus distressed firms).

Table 4 shows the results of firm performance before and after the organizational change in terms of the cross-sectional means and standard errors for each of our three measures. The difference between the pre- and post-change measures is also reported along with a t-statistic which tests for differences in the means.

Put Table 4 here

In terms of our overall sample, net income increased from -\$7.45 million prior to the organizational change to -\$0.24 million after the change on average. The cumulative abnormal returns also increase after a change in organizational form rising to 3.73% from minus 36.05% in the pre-change period. However, the return on assets remained relatively constant. Thus, on average, firms tend to become more profitable and increase the value of their equity after they switch organizational forms.

⁸Total assets is used to scale operating income to account for skewed dollar values arising from a few larger REITs.

⁹The betas used to calculate the abnormal returns are taken from the 250 trading days before the pre-change and post-change periods. The pre-change period begins 521 days before the firm restructuring and

When firm performance is evaluated relative to firm status, firms in financial distress show a dramatic improvement in profitability after organizational restructuring (to a looser form) regardless of the performance measure used. While non-distressed firms also exhibit increased performance on a post-change basis, the improvement is not as significant. Firm performance also increases, in general, relative to changes in firm structure (tighter vs. looser). Non-distressed firms moving to a tighter structure experience a significant increase in net income. These firms also have a higher return on assets and cumulative average returns after the reorganization although the improvement is not as notable. The increase on all three performance measures is relatively smaller and not significant with respect to non-distressed firms moving to a looser structure. This suggests that these firms may be relatively less healthy at the time of the change. To lessen our exposure to any changes that might affect all REITs, we corrected for changes in profitability for all REITs during each year and then performed the same analysis.¹⁰ The results of this correction are similar.

The preceding evidence on relative firm performance after an organizational change is consistent with the hypothesis that organizational changes are made with stockholder wealth maximization in mind and suggest that positive stock price reaction to announcements of these changes is justified by subsequent performance.

These results are reinforced when we regress the changes in profitability against both sub-classifications, firms switching to looser-versus-tighter structures and non-distressed versus distressed firms.

ends 21 days prior to the change. The post-change period starts 21 days after the organizational change and goes through until 521 days after the change.

¹⁰For example, if REITs are more likely to shift to a looser structure just before economic recoveries, any increase in profitability after the change will arise in part due to an economic upturn and not the organizational change per se. This correction should also significantly reduce any autocorrelation that might exist in the annual data for individual firms.

$$\text{DETA} = -0.0199 \quad + \quad 0.0266 \text{ NDIST} \quad + 0.0274 \text{ TIGHT} \quad \dots\dots\dots (3)$$

(1.48) (1.57) (0.89)

$$\text{DROA} = 0.0009 \quad - \quad 0.0089 \text{ NDIST} + 0.0026 \text{ TIGHT} \quad \dots\dots\dots (4)$$

(0.06) (0.43) (0.07)

^a Significant at the 1% level

DETA = Change in net income / total assets ($\text{NI/TA}_{\text{post}} - \text{NI/TA}_{\text{pre}}$)

DROA = Change in return on assets ($\text{EBIT/TA}_{\text{post}} - \text{EBIT/TA}_{\text{pre}}$)

NDIST= zero if firm is distressed; one if firm is non-distressed.

TIGHT= zero if firm shifts to a looser structure; one if firm shifts to a tighter structure.

There are no significant differences on either profitability measure between non-distressed and distressed firms, or among firms moving to a tighter or looser structure. Thus, all types of organizational changes, whether from a looser to a tighter structure or vice versa, seem to improve profitability. This finding is consistent with our argument that organizational changes in both directions are in the best interests of stockholders.

In summary, after making organizational changes, non-distressed firms that move to a tighter structure and distressed firms that move to a looser structure become more profitable and increase the value of their equity. Non-distressed firms moving to a looser structure do not do as well in terms of improving net income or return on assets, but they also increase the value of their equity in the aftermath of the change. The differences between distressed and non-distressed firms are neither dramatic nor statistically significant. Furthermore, non-distressed firms with high levels of operating income are much more likely to switch to a tighter structure to obtain the lower agency costs and the tax advantages associated with these organizational forms. All of the evidence is consistent with the hypothesis that organizational changes are made with stockholder wealth maximization in mind, and suggest that the positive stock price reaction to announcements of these changes is justified by subsequent performance.

3.5. Comparison of Firms that changed and those that did not

There is one final component to the puzzle that we have not adequately addressed in our empirical tests. We have shown that firms moving to both a tighter and looser structures had positive stock price reactions, on average. Both groups also registered an improvement in operating performance after the change. We have argued that these results are consistent with the interests of stockholders being served, but we cannot make claims about stockholder wealth maximization in the population, unless we can show that the firms that did not make organizational changes were also justified in their actions. In particular, given the characteristics of firms moving to a looser structure that we described in section 3.2, did all the firms that should have changed do so? The same question can be asked of the firms moving to a tighter structure.

To answer this question, we collected information on all real estate firms¹¹ in a looser structure (corporations) each year from 1976 to 1991, and compared them to the firms in the group that switched to a tighter structure over the same period. We similarly collected information on all REITs from 1976 to 1991, and compared them to REITs that did switch to a looser structure. In making the comparison, we looked at many of the dimensions that we considered earlier when comparing firms that switched to a looser as opposed to firms that switched to a tighter structure – profitability, leverage, dividend yield, and cash flow generating capacity. Table 5 summarizes the statistics for the firms that did and the firms that did not change that organizational form, based on whether the change is to a tighter or to a looser structure, during the period of our analysis.

Put Table 5 here

In the comparison of the REITs that switched to a looser structure to those that did not switch over the period, we find that the REITs that changed to a looser structure were smaller, significantly less profitable, were less leveraged and had less cash flow

¹¹ We look at all real estate corporations each year (in sic codes 6512 and 6513) as real estate firms in a looser structure.

generation at the time of the switch than the REITs that did not. This is consistent with our earlier findings that financial distress is behind the organizational change to a looser structure.

In the comparison of real estate corporations that changed to a tighter structure (mostly REITs) to the real estate corporations that did not make this switch, we find that the firms that switched were smaller, significantly more profitable, paid higher dividends and had higher free cash flow generating capacity than the firms that did not change organizational form. This again is consistent with our earlier finding that firms that move to a tighter structure are doing so because of the tax liabilities generated for investors in these companies by the high cash flows and dividends.

This evidence is consistent with the notion that the behavior of real estate firms, as a group, is consistent with stockholder wealth maximization, and that the firms that we would expect to change organizational form, for the most part, do so.

4. Discussion of results

The evidence presented here is consistent with the hypothesis that organizational form changes are motivated primarily by stockholder wealth maximization, although managers may still receive side-benefits from such changes. The positive stock price reaction to the announcement of the organizational form change and the subsequent increase in profitability and wealth, provide consistent evidence.

At the other extreme, firms with large free cash flows and relatively high dividend yields switch from a looser to a tighter structure. They find the tax benefits and reduction in agency costs are large enough to justify the loss of flexibility associated with these changes. Here again, the market reaction is positive, and these firms also become more profitable and wealthy.

5. Summary

This paper explores whether changes in organizational form by real estate firms are motivated primarily by the desire to increase stockholder wealth or to serve managerial interests. To address this issue, we stratify our sample of organizational changes along two dimensions: (1) Whether the change is to a looser or a tighter structure, and (2) whether the firm is in financial distress or not at the time of the change in organizational form. We conduct four tests of the competing hypotheses.

First, we examine the characteristics of firms moving to tighter and looser structures and find that firms which are in financial distress are more likely to move to a looser structure, whereas firms which have higher earnings and cash flows are more likely to move to a tighter structure. This, we argue, is more consistent with organizational changes being made to maximize stockholder wealth. We also find that the firms that move to a tighter structure have much higher insider holdings, which may explain why managers at these firms are much more willing to accept the move which gives them less discretionary power.

Second, we examine the stock price reaction to the announcement of the organizational changes. For the entire sample as well as the subsamples, there is a positive effect on stock prices when there are announcements of board approvals of the changes in organizational form. This would support the contention that stockholders, on average, perceive organizational changes as being positive in terms of their wealth effects. We also find that these positive abnormal returns persist when we categorize the firms, based upon whether management compensation increases or decreases in the year after the organizational change. This would support the notion that higher managerial compensation, when it does occur after an organizational change, is not coming at the expense of stockholder wealth.

Third, we document the changes in equity value and other performance measures that accompany the organizational form changes. We find evidence of increased equity value and improvement in earnings for non-distressed firms moving to a tighter structure

and troubled firms moving to a looser structure, with the increase being more dramatic for the latter group. This would suggest that the initial positive stock price response to the announcements is substantiated by the subsequent increase in profitability and stockholder wealth.

Finally, we look at the firms that did not make the organizational change and establish that these firms differed significantly, on average, from the firms that did change in terms of profitability, cash flows and financial health.

In summary, we find evidence consistent with the notion that organizational form changes in the sample of real estate firms that we examined were motivated primarily by the desire to increase stockholder wealth. While managerial self-interest may also have been served in the process, this has not come at the expense of the stockholders.

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Table 1: Insider Holdings at Real Estate Firms That Changed Organizational Form

This table summarizes insider holdings at the time of the organizational change for firms that moved from a looser to a tighter structure and for firms that moved from a tighter to a looser structure. The data on insider holdings is obtained from the SEC filings made by insiders at these firms; insiders are defined to include managers, directors and any investor holding more than a 5% interest in the firm.

	<i>Firms that move from a looser to tighter structure</i>	<i>Firms that move from a tighter to looser structure</i>
Average	26.97%	11.14%
Standard Deviation	14.98%	15.99%
Median	25.94%	2.55%
Distribution of Holdings		
< 5%	2	60
5%- 15%	3	12
15% - 25%	3	9
25% - 35%	5	8
> 35%	6	11

Table 2: Abnormal returns around organizational changes.

The announcement date is day 0 for the first event study; the date of the change is day 0 for the second event study; excess returns are estimated relative to the market model with parameters estimated from 200 trading days starting 210 days before and ending 21 days after the change. Panel A reports daily returns for the 5 days before and after the announcement day, while panel B reports the monthly returns for the 12 months before and after the announcement month. Cross-sectional standard errors are used to calculate t-statistics, which are reported in parentheses under the cross-sectional means. The bias-adjusted returns are estimated using the limited dependent variable technique.

Event day	Board approval date ¹				Shareholder approval date ²			
	To tighter structure	To looser structure Non-distr.	structure Distressed	All firms	To tighter structure	To looser structure Non-distr.	structure Distressed	All firms
# of firms	13	44	38	95	13	44	38	95
Panel A: Daily returns								
-5	-0.67% (-1.52)	-0.50% (-1.39)	-0.88% (1.62)	-0.62% (-1.42)	-1.94% (-1.41)	-0.02% (-0.05)	-0.69% (-1.68)	-0.35% (-1.25)
-4	0.20% (0.81)	-0.19% (-0.44)	0.27% (0.29)	-0.03% (-0.07)	0.19% (1.43)	0.27% (0.45)	0.79% (0.97)	0.38% (0.86)
-3	0.25% (0.34)	1.41% (1.16)	1.98% (2.59) ^a	1.48% ^a (2.08)	1.60% (1.61)	1.56% ^a (2.19)	1.28% (1.79) ^b	1.19% ^a (1.98)
-2	0.56% (0.63)	-0.37% (-1.18)	-1.17% (-0.75)	-0.52% (-1.07)	1.36% (1.45)	-0.72% ^b (-1.86)	-0.10% (-0.06)	-0.39% (-0.78)
-1	1.06% ^b (1.76)	-0.64% (-0.93)	0.52% (0.75)	-0.17% (-0.35)	-0.92% (-0.91)	-0.40% (-0.55)	0.61% (0.83)	-0.16% (-0.30)
0	1.16% ^b (1.89)	1.49% ^b (1.80)	2.61% ^a (2.03)	1.78% ^a (2.05)	0.69% (0.86)	-0.03% (-0.08)	2.53% ^b (1.87)	0.74% (1.60)
1	3.80% (1.38)	0.69% (1.34)	-0.24% (-0.35)	0.69% (1.54)	-0.42% (-0.89)	0.36% (0.75)	-0.44% (-0.68)	0.08% (0.22)
2	-1.19% (-0.83)	-0.50% (-0.98)	-0.17% (-0.15)	-0.46% (-1.01)	1.39% (1.68)	-0.26% (-0.52)	-1.27% (-1.35)	-0.41% (-0.99)
3	-1.50% (-1.30)	0.81% (1.03)	-0.03% (-0.07)	0.38% (0.73)	0.58% (0.44)	0.99% (1.27)	-0.30% (-0.68)	0.60% (1.13)
4	-0.76% (-1.24)	0.33% (1.25)	1.01% (1.12)	0.43% (1.15)	-0.47% (-1.43)	0.01% (0.02)	1.41% (1.17)	0.36% (1.03)
5	1.79% ^a (2.16)	-0.58% (-1.32)	0.33% (0.70)	-0.12% (-0.47)	-0.71% (1.12)	-0.74% ^b (-1.82)	-0.34% (-0.60)	-0.63% (-1.44)
0 to 1	4.96% ^b (1.75)	2.18% ^b (1.68)	2.37% ^b (1.81)	2.47% (1.92)	0.27% (0.15)	0.33% (0.80)	2.09% ^b (1.70)	0.82% (1.25)
-5 to +5	4.71% ^a (2.05)	1.97% ^b (1.82)	4.23% ^a (2.15)	2.84% ^a (2.03)	0.98% (0.91)	1.02% (0.77)	2.48% ^b (1.88)	1.02% (0.85)
-5 to +5	4.36% ^b (1.86)	1.48% ^b (1.74)	4.19% ^a (2.04)	2.75% ^b (1.89)	-0.81% (-0.57)	1.69% (1.33)	1.99% (1.32)	0.99% (0.74)
Bias Adj.								
Panel B: Monthly returns								
-12 TO -1	-0.55% (1.55)	-2.12% ^a (2.69)	-4.85% ^a (3.15)	-3.01% ^a (2.25)	-0.53% (1.51)	-2.11% ^a (2.35)	-4.79% ^a (3.07)	-2.96% ^a (2.59)
+1 to +12	0.09% (0.56)	0.33% ^b (1.66)	0.36% ^a (1.84)	0.31% ^b (1.74)	0.10% (0.45)	0.31% ^b (1.68)	0.35% ^b (1.80)	0.30% ^b (1.69)

^a Significant at 0.01 level^b Significant at 0.05 level¹ The board approval date is the day on which the board of directors approve of the organizational change.² The shareholder approval date is the day on which the shareholders approve of the organizational change. It happens after the board approval.

Table 3: Abnormal returns around Board Announcements of Organizational Changes: Management Compensation Classes.

The announcement date is day 0 for the event study; excess returns are estimated relative to the market model with parameters estimated from 200 trading days starting 210 days before and ending 21 days after the change. Cross-sectional standard errors are used to calculate t-statistics, which are reported in parentheses under the cross-sectional means. The bias-adjusted returns are estimated using the limited dependent variable technique.

Event Period	Management Compensation Increases	Management Compensation Decreases	Difference Between Groups
Number of Firms	49	46	
-5	-0.57% ^a (2.16)	-0.48% (1.51)	-0.09% (0.22)
-4	0.29% (0.75)	0.12% (0.24)	0.17% (0.25)
-3	1.89% ^a (4.10)	1.14% ^a (4.77)	0.75% (0.88)
-2	-0.33% (0.93)	-0.73% (1.08)	0.40% (0.52)
-1	1.05% ^a (2.32)	-0.21% (1.24)	1.36% ^a (2.61)
0	1.11% ^a (2.02)	1.85% ^a (1.95)	-0.74% (0.68)
+1	0.46% (0.93)	0.52% (1.38)	-0.06% (0.10)
+2	-0.64% (1.51)	-0.36% (0.69)	-0.28% (0.41)
+3	0.18% (0.61)	-0.54% ^a (2.03)	0.72% ^b (1.81)
+4	0.25% (0.89)	0.54% (1.10)	-0.29% (0.52)
+5	0.18% (0.75)	-0.10% (0.28)	-0.28% (0.74)
0 to 1	2.62% ^a (3.24)	2.16% ^b (1.73)	0.46% (0.31)
-5 to +5	3.87% ^a (2.72)	2.13% ^b (1.71)	1.74% (0.69)
-5 to +5 (Bias Adjusted)	3.75% ^a (2.56)	2.15% ^b (1.74)	1.60% (0.71)

^a Significant at 0.01 level

^b Significant at 0.05 level

¹ The board approval date is the day on which the board of directors approve of the organizational change.

Table 4: Performance measures around organizational changes.

The year in which the organization change is made is year 0. The performance measures are for the two years before (pre-change) and the two years after (post-change) the organizational change. The firms are classified on the basis of structural change (looser vs. tighter structures) and firm health (non-distressed vs. distressed firms). The cross-sectional standard errors are reported in brackets below the cross-sectional averages. The return on assets is the earnings before interest and taxes divided by the total assets. The cumulative abnormal returns are estimated for day -520 to day -21 for the pre-change period and day +21 to day +520 for the post-change period. The betas are estimated over the 250 trading days preceding each period.

	# Reports	Net Income (in \$)			Return on Assets (in %)			CAR (in %)		
		Pre-Change	Post-Change	Difference	Pre-Change	Post-Change	Difference	Pre-Change	Post-Change	Difference
<i>Non-distressed firms to</i>										
Looser	44	-0.85 ^b (0.45)	-0.66 (0.53)	0.20 (1.56)	4.01% ^a (3.20)	4.46% ^a (4.41)	0.40% (0.25)	-25.55% (2.62)	4.01% (0.44)	28.33% ^a (2.01)
Tighter	13	-0.43 (1.00)	9.83 ^a (2.71)	9.36 ^a (2.21)	10.15% ^a (3.86)	11.68% ^a (3.66)	0.14% (0.05)	-6.65% (0.60)	1.06% (0.15)	7.71% (1.05)
<i>Looser vs. Tighter</i>										
t-stat				1.90 ^b			0.44			1.86 ^b
z-stat				1.88 ^b			1.38			1.95 ^b
<i>Firm Status</i>										
Non-distressed	57	-0.73 (0.43)	1.38 (1.07)	2.78 ^b (1.87)	6.81% ^a (6.25)	7.07% ^a (8.32)	0.26% (0.19)	-22.07% ^a (2.29)	3.60% (0.40)	25.56% (1.85)
Distressed	38	-14.44 ^a (3.09)	-2.42 (1.16)	12.02 ^a (2.20)	1.74% (1.46)	4.39% ^a (3.01)	2.66% ^b (1.95)	-58.19% ^a (2.51)	4.10% (0.27)	58.80% ^a (2.68)
<i>Non-dist vs. Distressed</i>										
t-stat				1.80 ^b			2.01 ^a			1.09
z-stat				1.53			2.46 ^a			1.17
<i>All Firms</i>	95	-7.45 ^a (2.95)	-0.29 (0.25)	7.03 ^a (2.70)	4.37% (5.20)	4.42% (5.52)	0.05% (0.04)	-36.05% (3.31)	3.73% (0.47)	37.96% ^a (2.58)

^a Significant at 0.01 level ^b Significant at 0.05 level

¹ The t-statistic tests the hypothesis that the means of the two groups are equal.

² The z-statistic is a nonparametric median test, based upon the number of points above the median.

³ A change is classified as a shift to a looser (tighter) structure if it leads to a structure with fewer (more) constraints on capital structure, dividend policy and asset sales.

Table 5: Firms that Changed Organizational Form Versus Firms That Did Not Change Form

The firms are classified on the basis of structural change (looser vs. tighter structures) and compared to real estate firms that did not change organizational form between 1976 and 1992. For the firms moving to a looser structure, the comparison is made with REITs that did not change organizational form. For firms moving to a tighter structure, the comparison is made with real estate corporations that did not change organizational form. The standard errors are reported in brackets below the cross-sectional averages. The cumulative abnormal returns are estimated for day -520 to day -21 for the pre-change period and day +21 to day +520 for the post-change period. The t-statistic tests the hypothesis that the means of the two groups are equal. The z-statistic is a nonparametric median test, based upon the number of points above the median.

	<i>To Looser Structure</i>		<i>Change vs. No Change</i>		<i>To Tighter Structure</i>		<i>Change vs No Change</i>	
	<i>Change</i>	<i>No Change</i>	<i>T Statistic</i>	<i>Z Statistic</i>	<i>Change</i>	<i>No Change</i>	<i>T Statistic</i>	<i>Z Statistic</i>
# of Firms	101	1230			16	448		
Total Assets (TA)	144.58 (41.34)	235.67 (17.27)	2.03 ²	1.96 ^a	87.01 (23.07)	255.30 (49.94)	3.05 ^a	2.54 ^a
Earnings/TA	-2.95% (0.97%)	2.44% (0.49%)	4.96 ^a	6.72 ^a	5.67% (1.33%)	2.18% (1.11%)	3.38 ^a	2.92 ^a
Debt/TA	28.73% (2.79%)	33.81% (0.78%)	1.75 ^b	2.79 ^a	28.22% (8.03%)	33.83% (1.24%)	0.69	0.84
Dividend Yield	9.75% (2.35%)	10.80% (1.50%)	0.38	0.59	2.75% (1.16%)	1.78% (1.12%)	1.85 ^b	1.86 ^b
FCF/TA	3.08% (1.16%)	6.24% (0.44%)	2.54 ^a	5.36 ^a	11.07% (3.10%)	5.60% (0.47%)	1.74 ^b	1.92 ^b

^a Significant at 0.01 level

^b Significant at 0.05 level